DEPARTMENT OF STATE REVENUE

02-20182181.LOF

Letter of Findings Number: 02-20182181
Corporate Income Tax
For Tax Years 2013, 2014, 2015, and 2016

NOTICE: IC § 6-8.1-3-3.5 and IC § 4-22-7-7 requires the publication of this document in the Indiana Register. This document provides the general public with information about the Department's official position concerning a specific set of facts and issues. This document is effective on its date of publication and remains in effect until the date it is superseded or deleted by the publication of another document in the Indiana Register. The "Holding" section of this document is provided for the convenience of the reader and is not part of the analysis contained in this Letter of Findings.

HOLDING

Indiana Company's sales made in 2013, 2014, and 2015 to Florida, Georgia, Louisiana, North Carolina, Ohio, Tennessee, and Washington, as well as those sales made in 2015 in Texas, and 2014 and 2015 in Virginia should be excluded from the numerator of Company's apportionment formula. However, Company's 2013, 2014, and 2015 sales to Canada, Illinois, and New York, as well as those sales made to Texas in 2013 and 2014, and sales made to Virginia in 2013 are properly included in the numerator of Company's apportionment formula. Further, waiver of penalty is warranted.

ISSUES

I. Income Tax–Throwback Sales.

Authority: 15 U.S.C. § 381; IC § 6-3-2-2; IC § 6-8.1-5-1; IC § 6-3-1-25; *Indiana Dep't of State Revenue v. Rent-A-Center East, Inc*., 963 N.E.2d 463 (Ind. 2012); *Lafayette Square Amoco, Inc. v. Indiana Dep't of State Revenue,* 867 N.E.2d 289 (Ind. Tax Ct. 2007); *Scopelite v. Indiana Dep't of Local Gov't Fin.*, 939 N.E.2d 1138 (Ind. Tax Ct. 2010); *Wendt LLP v. Indiana Dep't of State Revenue*, 977 N.E.2d 480 (Ind. Tax Ct. 2012); *Indiana Dep't of State Rev. v. Caterpillar, Inc.*, 15 N.E.3d 579, 583 (Ind. 2014); *Sherwin-Williams Co. v. Indiana Dep't of State Revenue*, 673 N.E.2d 849 (Ind. Tax Ct. 1996); *Wisconsin Dep't of Revenue v. William Wrigley, Jr., Co.*, 505 U.S. 214 (1992); *Indiana Dep't of State Revenue v. Kimberly-Clark Corp.*, 416 N.E.2d 1264 (Ind. 1981); *Welch Packaging Group, Inc. v. Indiana Dept. of State Revenue*, 876 N.E.2d 819 (Ind. Tax Ct. 2007); 45 IAC 3.1-1-35; 45 IAC 3.1-1-38; 45 IAC 3.1-1-53; 45 IAC 3.1-1-64; United States - Canada Income Tax Convention, U.S.-Ca., Sep. 26, 1980, T.I.A.S 11,087; Fla. Stat. § 220.11; Fla. Admin. Code r. 12C-1.011; Ga. Code. Ann., § 48-7-31; Ga. Comp. R. & Regs. 560-7-7-.03; 35 Ill. Comp. Stat. § 5/201; Ill. Admin. Code tit. 86, § 100.9720; La. Rev. Stat. Ann. § 47:287.11; La. Rev. Stat. Ann. § 47:287.95; La. Rev. Stat. Ann. § 47.601; La. Admin. Code tit. 61, Pt. 1, §1134; N.Y. Tax Law § 209; 20 NYCRR § 1-3.2; N.C. Gen. Stat. § 105-130.3; 17 N.C. Admin. Code 5C.0101; 17 N.C. Admin. Code 5C.0102; 17 N.C. Admin. Code 5C.0103; Ohio. Rev. Code Ann. §5751.02; Ohio. Rev. Code Ann. §5751.03; Ohio. Rev. Code Ann. §5751.01; Tenn. Code Ann. § 67-4-2005; Tenn. Code Ann. § 67-4-2007; Tenn. Code Ann. § 67-4-2004; Tenn. Code Ann. § 67-4-2105; Tenn. Code Ann. § 67-4-2106; Tex. Tax Code § 171.001; Tex. Tax Code § 171.0002; Tex. Tax Code § 171.002; Tex. Tax Code §171.0004; Tex. Tax Code § 171.106; Tex. Admin. Code § 3.586; Va. Code Ann. § 58.1-400; Va. Code Ann. § 58.1-441; 23 Va. Admin. Code § 10-120-70; 23 Va. Admin. Code § 10-120-310; Wash. Rev. Code § 82.04.220; Wash. Rev. Code § 82.04.066; Wash. Rev. Code § 82.04.067; Black's Law Dictionary 1497 (10th ed. 2014).

Taxpayer maintains that sales to customers in certain jurisdictions should not be thrown back to Indiana because Taxpayer has nexus in each jurisdiction.

II. Tax Administration–Negligence Penalty.

Authority: IC § 6-8.1-10-2.1; 45 IAC 15-11-2

Taxpayer protests the imposition of a ten percent negligence penalty.

STATEMENT OF FACTS

Taxpayer is a manufacturer of industrial products for a variety of industries, including the automotive and manufacturing industries. Taxpayer is headquartered in and has a manufacturing facility in Indiana.

Taxpayer files as a member of a consolidated federal return, but files as a separate filer for Indiana purposes. On October 13, 2017, Taxpayer filed an amended Indiana corporate return for the tax year ending December 31, 2013. That amended return resulted in a refund request because "[TP] determined it created income/franchise tax nexus in additional states for 2013 because of business activities conducted in jurisdictions . . . ."

The review of the amended return led the Indiana Department of Revenue ("Department") to conduct a corporate income tax audit for Taxpayer for tax years 2013, 2014, 2015, and 2016. The audit found that certain sales to states with which Taxpayer did not have nexus had not been included in the numerator for apportioning Indiana sales. Therefore, the Department threw those sales back to Indiana, resulting in a denial of the refund claimed for 2013, and an assessment of additional income tax for 2014 and 2015.

Taxpayer filed a timely protest of the Department's audit. An administrative hearing was conducted during which Taxpayer explained the basis for its protest. This Letter of Findings results. Additional facts will be provided as necessary.

I. Income Tax– Throwback Sales.

DISCUSSION

Pursuant to an audit, the Department included certain sales to outside jurisdictions in Taxpayer's Indiana adjusted gross income. Specifically, the audit determined that Taxpayer did not have nexus with these locations and its income derived from sales to those locations were not subject to tax in those jurisdictions under P.L. 86-272. The audit thus applied the Indiana throwback rule, which resulted in additional Indiana income tax for the tax years at issue.

Taxpayer disagrees with the audit results as it pertains to the following jurisdictions: Canada; Florida; Georgia; Illinois; Louisiana; New York; North Carolina; Ohio; Tennessee; Texas; Virginia; and Washington. Taxpayer asserts that it had nexus with each of these jurisdictions because its activities constituted "doing business" in the jurisdiction and are therefore protected activities under P.L. 86-272. Thus, Taxpayer maintains that the Indiana throwback rule is not applicable to sales in these jurisdictions.

As a threshold issue, it is the taxpayer's responsibility to establish that the existing tax assessment is incorrect. As stated in IC § 6-8.1-5-1(c), "The notice of proposed assessment is prima facie evidence that the department's claim for the unpaid tax is valid. The burden of proving that the proposed assessment is wrong rests with the person against whom the proposed assessment is made." *Indiana Dep't of State Revenue v. Rent-A-Center East, Inc.*, 963 N.E.2d 463, 466 (Ind. 2012); *Lafayette Square Amoco, Inc. v. Indiana Dep't of State Revenue*, 867 N.E.2d 289, 292 (Ind. Tax Ct. 2007). Thus, the taxpayer is required to provide documentation explaining and supporting its challenge that the Department's assessment is wrong. Poorly developed and non-cogent arguments are subject to waiver. *Scopelite v. Indiana Dep't of Local Gov't Fin.*, 939 N.E.2d 1138, 1145 (Ind. Tax Ct. 2010); *see also Wendt LLP v. Indiana Dep't of State Revenue,* 977 N.E.2d 480, 486 n.9 (Ind. Tax Ct. 2012). When an agency is charged with enforcing a statute, the jurisprudence defers to the agency's reasonable interpretation of that statute "over an equally reasonable interpretation by another party." *Indiana Dep't of State Rev. v. Caterpillar, Inc.*, 15 N.E.3d 579, 583 (Ind. 2014).

For purposes of this discussion, it is important to note that under IC § 6-3-1-25 and 45 IAC 3.1-1-35, "state" is defined as "any state of the United States, the District of Columbia, the Commonwealth of Puerto Rico, any territory or possession of the United States, and **any foreign country** or political subdivision thereof." (**Emphasis added**).

"Indiana imposes a tax on every corporation's adjusted gross income derived from sources within Indiana. [IC § 6-3-2-1(b).] In cases where a corporation derives business income from sources both within and without Indiana, the 'adjusted gross income derived from sources within the state of Indiana is determined by an apportionment formula.'" *Sherwin-Williams Co. v. Indiana Dep't of State Revenue*, 673 N.E.2d 849, 851 (Ind. Tax Ct. 1996). For all tax years after December 31, 2010, that formula operates by multiplying taxpayer's total business income by a fraction composed of a sales factor. IC § 6-3-2-2(b)(5). The "sales factor" consists of a fraction, "the numerator of which is the total sales of the taxpayer in [Indiana] during the taxable year, and the denominator of which is the total sales of the taxpayer everywhere during the taxable year." IC § 6-3-2-2(e). The basic rule for calculating the sales factor is found at IC § 6-3-2-2. IC § 6-3-2-2(e) provides that "[s]ales of tangible personal property are in this state if . . . (2) the property is shipped from an office, a store, a warehouse, a factory, or other place of storage in this state and . . . (B) the taxpayer is not taxable in the state of the purchaser."

IC § 6-3-2-2(a), in pertinent part, states that Indiana taxpayers are subject to this state's income tax on money earned from doing business within this state:

> (a) With regard to corporations and nonresident persons, "adjusted gross income derived from sources within Indiana", for the purposes of this article, shall mean and include:
> (1) income from real or tangible personal property located in this state;
> (2) income from doing business in this state;
> (3) income from a trade or profession conducted in this state;
> (4) compensation for labor or services rendered within this state; and
> (5) income from stocks, bonds, notes, bank deposits, patents, copyrights, secret processes and formulas, good will, trademarks, trade brands, franchises, and other intangible personal property to the extent that the income is apportioned to Indiana under this section or if the income is allocated to Indiana or considered to be derived from sources within Indiana under this section.

However, IC § 6-3-2-2(n) provides that a taxpayer's income is not subject to Indiana's income tax if that income is attributable to doing business in another state in which it is subject to that foreign state's own tax regime:

> (n) For purpose of allocation and apportionment of income under this article, a taxpayer is taxable in another state if:
> (1) in that state the taxpayer is subject to a net income tax, a franchise tax measured by net income, a franchise tax for the privilege of doing business, or a corporate stock tax; or
> (2) that state has jurisdiction to subject the taxpayer to a net income tax regardless of whether, in fact, the state does or does not.

45 IAC 3.1-1-38 explains the "doing business" in a foreign state principle:

> For apportionment purposes, a taxpayer is "doing business" in a state if it operates a business enterprise or activity in such state including, but not limited to:
>
> (1) Maintenance of an office or other place of business in the state.
> (2) Maintenance of an inventory of merchandise or material for sale distribution, or manufacture, or consigned goods.
> (3) Sale or distribution of merchandise to customers in the state directly from company-owned or operated vehicles where title to the goods passes at the time of sale or distribution.
> (4) Rendering services to customers in the state.
> (5) Ownership, rental or operation of a business or of property (real or personal) in the state.
> (6) Acceptance of orders in the state.
> (7) Any other act in such state which exceeds the mere solicitation of orders so as to give the state nexus under P.L. 86-272 to tax its net income.
>
> As stated in Regulation 6-3-2-2(b)(010) [45 IAC 3.1-1-37], corporations doing business in Indiana as well as other states are subject to the allocation and apportionment provisions of IC 6-3-2-2(b)-(n).

45 IAC 3.1-1-64, in relevant part, further illustrates under what conditions a taxpayer is "doing business" and is therefore taxable in another state:

> A corporation is "taxable in another state" under the Act when such state has jurisdiction to subject it to a net income tax. This test applies if the taxpayer's business activities are sufficient to give the state jurisdiction to impose a net income tax under the Constitution and statutes of the United States. **Jurisdiction to tax is not present where the state is prohibited from imposing the tax by reason of the provision of Public Law 86-272, 15 U.S.C.A. §381-385**. In the case of any "State," as defined in IC 6-3-1-25, other than a state of the United States or political subdivision of such state, the determination of whether such "state" has jurisdiction to subject the taxpayer to a net income tax shall be made by application of the jurisdictional standards applicable to that state of the United States. If jurisdiction to tax is otherwise present, such "state" is not considered as being without jurisdiction to tax by reason of the provisions of a treaty between that state and the United States.
>
> Example:
>
> Corporation X is actively engaged in manufacturing farm equipment in State A and foreign country B. Both State A and foreign country B impose a net income tax but foreign country B exempts corporations engaged

> in manufacturing farm equipment. Corporation X is subject to the jurisdiction of State A and foreign country B.
>
> **Taxpayers are not subject to throwback on sales into states in which they are taxable under this regulation** [45 IAC 3.1-1-64]. See Regulation 6-3-2-2(e)(040) [45 IAC 3.1-1-53].
>
> (**Emphasis added**).

45 IAC 3.1-1-53 describes the "throw back" principle:

> Gross receipts from the sales of tangible personal property (except sales to the United States Government-See Regulation 6-3-2-2(e)(050) [45 IAC 3.1-1-54] are in this state: (a) if the property is delivered or shipped to a purchaser within this state regardless of the F.O.B. point or other conditions of sales; or (b) if the property is shipped from an office, store, factory, or other place of storage in this state, and the taxpayer is not taxable in the state of the purchaser. See Regulation 6-3-2-2(n)(010) [45 IAC 3.1-1-64].
>
> Examples:
> . . .
> (5) **If the taxpayer is not taxable in the state of the purchaser, the sale is attributed to this state if the property is shipped from an office, store, warehouse, factory, or other place of storage in this state. Such sale is termed a "Throwback" sale**. Example: The taxpayer has its head office and factory in State A. It maintains a branch office and inventory in Indiana. Taxpayer's only activity in State B is the solicitation of orders by a resident salesman. All orders by the State B salesman are sent to the branch office in Indiana for approval and are filled by shipment from the inventory in Indiana. Since the taxpayer is immune under P.L.86-272 from tax in State B, all sales of merchandise to purchasers in State B are attributed to Indiana, the state from which the merchandise was shipped.
> . . .
> (**Emphasis added**).

Accordingly, in every transaction, at least one state has the authority to impose tax on income derived from the sale of tangible personal property.

The issue at hand is whether Taxpayer's activities brought itself within the purview of Canada, Florida, Georgia, Illinois, Louisiana, New York, North Carolina, Ohio, Tennessee, Texas, Virginia, or Washington's income tax regimes. 15 U.S.C. § 381(a) (Public Law 86-272) establishes the minimum standards under which Indiana or any foreign state may permissibly impose tax. In relevant part, the law provides as follows:

> No State, or political subdivision thereof, shall have power to impose, for any taxable year ending after September 14, 1959, a net income tax on the income derived within such State by any person from interstate commerce if the only business activities within such State by or on behalf of such person during such taxable year are either, or both, of the following:
>
> (1) the solicitation of orders by such person, or his representative, in such State for sales of tangible personal property, which orders are sent outside the State for approval or rejection, and, if approved, are filled by shipment or delivery from a point outside the State; and
> (2) the solicitation of orders by such person, or his representative, in such State in the name of or for the benefit of a prospective customer of such person, if orders by such customer to such person to enable such customer to fill orders resulting from such solicitation are orders described in paragraph (1).

15 U.S.C. § 381(c) explains under which conditions a company is *not* conducting business in another state:

> For purposes of subsection (a) of this section, a person shall not be considered to have engaged in business activities within a State during any taxable year merely by reason of sales in such State, or the solicitation of orders for sales in such State, of tangible personal property on behalf of such person by one or more independent contractors, or by reason of the maintenance, of an office in such State by one or more independent contractors whose activities on behalf of such person in such State consist solely of making sales, or soliciting orders for sales, of tangible personal property.

Public Law 86-282 prohibits states from imposing a net income tax on a foreign taxpayer if the foreign taxpayer's only business activity within that state is the solicitation of sales. A state may not impose an income tax on income derived from business activities within that state unless those activities exceed the "mere solicitation" of sales.

The court in *Indiana Dep't of State Revenue v. Kimberly-Clark Corp.*, 416 N.E.2d 1264 (Ind. 1981), found that the nonresident taxpayer did not exceed solicitation of orders for sales in Indiana because it only employed salesmen who lived in Indiana to perform activities such as, checking inventories, checking shelf facings, and explaining products. *Id.* at 1266. The *Kimberly-Clark* court stated that "each case must be judged upon its own merits, with particular emphasis placed upon the totality of a corporation's activities within a state." *Id*. at 1268. The Kimberly-Clark court held that solicitation of orders for sales includes "sundry activities so long as those activities (are) closely related to the eventual sale of a product." *Id*. (Internal citation omitted). The Kimberly-Clark court concluded that the taxpayer's activities in Indiana were "inextricably related to solicitation" or as "acts of courtesy," and, therefore, the taxpayer was not taxable in Indiana. *Id*.

The U.S. Supreme Court refined the "mere solicitation" standard in *Wisconsin Dep't. of Revenue v. William Wrigley, Jr., Co.*, 505 U.S. 214 (1992). In *Wrigley*, the taxpayer, a manufacturer of chewing gum, claimed that P.L. 86-272 prohibited Wisconsin from taxing its income because (1) it did not have any office (or real estate) in Wisconsin and (2) its business activities in Wisconsin were within the scope of solicitation of orders and were *de minimis*. *Id*. at 235. The Court disagreed and, in relevant part, stated:

> We proceed, therefore, to describe what we think the proper standard to be. Once it is acknowledged, as we have concluded it must be, that "solicitation of orders" covers more than what is strictly *essential* to making requests for purchases, the next (and perhaps the only other) clear line is the one between those activities that are *entirely ancillary* to requests for purchases–those that serve no independent business function apart from their connection to the soliciting of orders–and those activities that the company would have reason to engage in anyway but chooses to allocate to its in-state sales force. Providing a car and a stock of free samples to salesmen is part of the "solicitation of orders," because the only reason to do it is to facilitate requests for purchases. Contrariwise, employing salesmen to repair or service the company's products is not part of the "solicitation of orders," since there is good reason to get that done whether or not the company has a sales force. Repair and servicing may help to *increase* purchases; but it is not ancillary to *requesting purchases*, and cannot be converted into "solicitation" by merely being assigned to salesmen.
>
> *Id*. at 228-29 (*Emphasis in original*) (Internal citation omitted).

The Court further explained:

> By contrast, Wrigley's in-state recruitment, training, and evaluation of sales representatives and its use of hotels and homes for sales-related meetings served no purpose apart from their role in facilitating solicitation. The same must be said of the instances in which Wrigley's regional sales manager contacted the Chicago office about "rather nasty" credit disputes involving important accounts in order to "get the account and [Wrigley's] credit department communicating." It hardly appears likely that this mediating function between the customer and the central office would have been performed by some other employee – some company ombudsman, so to speak – if the on-location sales staff did not exist. The purpose of the activity, in other words, was to ingratiate the salesman with the customer, thereby facilitating requests for purchases.
>
> Finally, Wrigley argues that the various nonimmune activities, considered singly or together, are *de minimis*. In particular, Wrigley emphasizes that the gum sales through "agency stock checks" accounted for only 0.00007 [percent] of Wrigley's annual Wisconsin sales, and in absolute terms amounted to only several hundred dollars a year. We need not decide whether any of the nonimmune activities was *de minimis* in isolation; taken together, they clearly are not. Wrigley's sales representatives exchanged stale gum, as a matter of regular company policy, on a continuing basis, and Wrigley maintained a stock of gum worth several thousand dollars in the State for this purpose, as well as for the less frequently pursued (but equally unprotected) purpose of selling gum through "agency stock checks." Although the relative magnitude of these activities was not large compared to Wrigley's other operations in Wisconsin, we have little difficulty concluding that they constituted a nontrivial additional connection with the State. Because Wrigley's business activities within Wisconsin were not limited to those specified in § 381, the prohibition on net-income taxation contained in that provision was inapplicable.

Id. at 234-5.

Ruling in favor of Wisconsin, the court thus held that the taxpayer in *Wrigley* was subject to Wisconsin's net income tax because its business activities in Wisconsin exceeded P.L. 86-272's protection. *Id.* at 235. Thus, following the *Wrigley* decision, an Indiana company's income derived from its sales to other states is thrown back to Indiana for income tax purposes when the Indiana company's business activities in those states are protected and are not taxable pursuant to P.L. 86-272.

In the instant case, Taxpayer manufactures industrial products for a variety of industries. Taxpayer argued that in each of the jurisdictions at issue, its activities exceeded mere solicitation of sales, and therefore were protected from throw back under P.L. 86-272. In its protest letter and during the administrative hearing, Taxpayer gave a detailed account of its activities in the contested jurisdictions. Each of those jurisdictions are discussed below:

Canada

The Department determined that Taxpayer's sales made to Canada were incorrectly excluded from the Indiana sales factor numerator for tax years 2013, 2014, and 2015. Taxpayer argues that its activities in Canada "constitute 'doing business in a state' under [45] IAC 3.1-1-38." Taxpayer argues that it created nexus in Canada in two ways. First, it ships products to Canada via returnable containers. These containers stay in Canada for three to six months before being returned to Taxpayer, thus, Taxpayer argues that it owned property in Canada. Second, Taxpayer argues that its activities in Canada exceeded mere solicitation of sales. These activities include "auditing production processes, performing maintenance, providing technical assistance for client machinery and operations, and discussing delinquent receivables."

To support its activities in Canada, Taxpayer provided the audit team with "travel receipts for airline, hotels, meals, . . . [and] business trip applications for Canada visits. The business trip applications had a brief description of the purpose of the trip." The audit found that "[n]one of the activities on the business trip applications exceed mere solicitation." Further, the audit report noted that no additional information such as case logs or meeting minutes "that would support activities by the representatives" were provided by Taxpayer.

During the administrative hearing, Taxpayer provided the Department with documentation supporting its activities in Canada for all three tax years at issue. For 2013 Taxpayer provided copies of meeting notes and quality control reports. These documents record and describe the results of a quality assurance audit. The meeting notes have some indication that Taxpayer employees would attend activities in Canada, but no proof that they actually did. The quality assurance audit is thorough, but does not show who performed the audit and when. For 2014 and 2015 Taxpayer provided the same type of documentation as well as their internal business trip applications and travel expense reports. These documents purport to prove that Taxpayer employees traveled to Canada, but there is no documentation to link the travel with the activities performed. For example, the 2014 business trip application indicates that Taxpayer employees would travel to Canada on December 1, 2014 - December 4, 2014, but the accompanying audit report indicates that the audit took place on January 22, 2014.

The Department does not find the presence of returnable containers akin to owning property in a given jurisdiction. Taxpayer has not provided evidence that the returnable containers were leased/rented by their customers and the temporary nature of the containers' presence does not lend itself to creating nexus in Canada. However, under Indiana law, if Taxpayer is traveling to Canada to perform audits, quality control tests, and the like, then unlike the taxpayer in *Kimberly-Clark*, Taxpayer's activities were not "inextricably related to solicitation" and were more than "acts of courtesy." Taxpayer's activities took place *because* of a sale; like the activities in *Wrigley*, the services may help increase purchases, but were not ancillary to requesting purchases. Therefore, the Department agrees that Taxpayer's purported activities in Canada could constitute doing business in Canada. However, Taxpayer has not provided sufficient documentation to support its claim under IC § 6-8.1-5-1(c).

Not only has Taxpayer not supported its activities in Canada, but because of the international nature of these transactions, the United States - Canada Income Tax Convention ("Convention") must be consulted. Under the Convention:

> The business profits of a resident of a Contracting State shall be taxable only in that State unless the resident carries on business in the other Contracting State through a permanent establishment situated therein. If the resident carries on, or has carried on, business as aforesaid, the business profits of the resident may be taxed in the other State but only so much of them as is attributable to that permanent establishment.
>
> United States - Canada Income Tax Convention, U.S.-Ca., Sept. 26, 1980, T.I.A.S 11,087, Article VII, Section 1.

Therefore, the business profits of Taxpayer are taxable only in Indiana unless Taxpayer conducts business in Canada through a permanent establishment. According to the Convention:

> [T]he term "permanent establishment" means a fixed place of business through which the business of a resident of a Contracting State is wholly or partly carried on. The term "permanent establishment" shall

include especially: (a) A place of management; (b) A branch; (c) An office; (d) A factory; (e) A workshop; and (f) A mine, an oil or gas well, a quarry or any other place of extraction of natural resources.

Id., Article V, Sections 1 & 2.

Moreover, "A person acting in a Contracting State on behalf of a resident of the other Contracting State . . . shall be deemed to be a permanent establishment in the first-mentioned State if such person has, and habitually exercises in that State, an authority to conclude contracts in the name of the resident. *Id*., Article V, Section 5.

Thus, under the Convention, Taxpayer's business profits are taxable in Canada if Taxpayer has a permanent establishment in Canada, which can be a physical location under Sections 1 and 2, or a person under section 5. Taxpayer does not maintain a physical location in Canada and Taxpayer has not provided sufficient evidence to show that they have an employee who functions in such a way as to create a permanent establishment in Canada under the Convention. Thus, Taxpayer is not taxable in Canada under the Convention.

Taxpayer has not provided sufficient evidence to show that it is "conducting business" in Canada under Indiana law, nor has it shown that it is taxable in Canada under the Convention, therefore Taxpayer's Canadian sales were properly thrown back to Indiana.

Florida

The Department determined that Taxpayer's sales made to Florida were incorrectly excluded from the Indiana sales factor numerator for tax year 2013. Taxpayer argues that it was conducting business in Florida under Florida and Indiana law and therefore was taxable in Florida. As such, Taxpayer believes that its Florida sales should not be included in the numerator of the Indiana sales factor under IC § 6-3-2-2(n).

Taxpayer states that the presence of its returnable containers in the state of Florida constitutes "doing business in another state" under 45 IAC 3.1-1-38(5). Further, Taxpayer explains that it "rendered services to Florida customers by testing and reviewing [Taxpayer] products to ensure compliance with machinery." Additionally, Taxpayer "employees visited customers in Florida to test [Taxpayer products] on machinery. . . . The purpose of this activity is to determine if [Taxpayer's] products work as expected on certain types of machinery. After running the test, [Taxpayer] employees returned to Florida to review and analyze the test results." Taxpayer believes that these services constitute "doing business" in Florida under 45 IAC 3.1-1-38(4).

In the administrative hearing, Taxpayer provided evidence that during 2013 it had an employee working from a home office in Florida. According to the audit report, employees working in states outside of Indiana are "account representatives" whose job is to "maintain contact with ongoing and potential customers." These employees work with customers with delinquent accounts, are present while customers dispose of obsolete inventory, are involved with contract negotiations, and communicate to customers whether or not an order is approved.

Florida imposes an income tax "for the privilege of conducting business, earning or receiving income in [Florida], or being a resident or citizen of [Florida]." Fla. Stat. § 220.11(1). According to Florida law "conducting business" includes, but is not limited to the following activities:

1. Assembling, installing, servicing, or repairing the taxpayer's products in Florida by its agents or employees.
2. Accepting orders in Florida by its employees.
3. Having employees that are present in Florida and that perform functions other than the solicitation of sales within Florida.
4. Performing any service within Florida.

Fla. Admin. Code r. 12C-1.011(1)(h), (i), (l), and (m).

As mentioned above, the Department does not find the presence of its returnable containers in Florida sufficient to create nexus in Florida. However, Taxpayer provided evidence that they had an employee working from his home in Florida and that that employee performed services in Florida that exceeded the solicitation of sales. Therefore, under Florida law, because Taxpayer is performing services in Florida, Taxpayer is subject to Florida tax. Indeed, Taxpayer filed a 2013 Florida Corporate Income/Franchise Tax Returns with substantial Florida income. As such, Taxpayer's Florida sales are not subject to the Indiana throwback rules. Taxpayer is sustained in regards to its Florida sales.

Georgia

The Department determined that Taxpayer's Georgia sales were incorrectly excluded from the Indiana sales factor numerator for tax years 2013 and 2014. Taxpayer contends that it was conducting business in Georgia under Georgia and Indiana law and therefore was taxable in Georgia. As such, Taxpayer believes that its Georgia sales should not be included in the numerator of the Indiana sales factor under IC § 6-3-2-2(n).

Taxpayer states that the presence of its returnable containers in the state of Georgia constitutes "doing business in another state" under 45 IAC 3.1-1-38(5). However, the Department does not find the presence of returnable containers in Georgia sufficient to create nexus in Georgia. Taxpayer also explains that "[Taxpayer] rendered services to Georgia customers by providing product quality review services. These quality review services included obtaining product samples for analysis and discussing trial testing results. . . . The purpose of these analyses is to ensure that [Taxpayer] products are working properly."

In the administrative hearing, Taxpayer provided evidence that during 2013 and 2014, it had an employee working from a home office in Georgia. According to the audit report, employees working in states outside of Indiana are "account representatives" whose job is to "maintain contact with ongoing and potential customers." These employees work with customers with delinquent accounts, are present while customers dispose of obsolete inventory, are involved with contract negotiations, and communicate to customers whether or not an order is approved.

Georgia imposes a tax upon the "entire net income . . . received by every foreign or domestic corporation owning property within [Georgia], doing business within [Georgia], or deriving income from sources within [Georgia] to the extent permitted by the United States Constitution." Ga. Code. Ann., § 48-7-31(a). "A corporation shall be deemed to be doing business within [Georgia] if it engages within [Georgia] in any activities or transactions for the purpose of financial profit or gain whether or not: (1) The corporation qualifies to do business in this state; (2) The corporation maintains an office or place of doing business within this state; or (3) Any such activity or transaction is connected with interstate or foreign commerce." *Id*.

The Georgia regulations interpret what "doing business within Georgia" means. Ga. Comp. R. & Regs. 560-7-7-.03(1) explains that:

> A corporation will be considered to be doing business within [Georgia] if it performs acts or consummates transactions within [Georgia] which result in financial profit or gain, or if it engages within [Georgia] in any activities or transactions for the purpose of financial profit or gain. A corporation will be considered to be engaged in an activity in [Georgia] whose agent, salesman, or other representative in whatever capacity, engages in solicitation, demonstration, taking of orders, collection activities, or any other activity for the purpose of financial profit or gain. . . .

Taxpayer provided evidence that they had an employee working from a home office in Georgia and that that employee performed services in Georgia that were predominantly sales and sales-related. Under Georgia law, based on the sales activities alone, Taxpayer is considered to be doing business in Georgia. In fact, Taxpayer filed Georgia Corporation Tax Returns with substantial Georgia income for each year at issue. As such, Taxpayer's Georgia sales are not subject to the Indiana throwback rules. Taxpayer is sustained in regards to its Georgia sales.

Illinois

The Department determined that Taxpayer's sales made to Illinois were incorrectly excluded from the Indiana sales factor numerator for tax year 2014. Taxpayer argues that it was conducting business in Illinois and therefore was taxable in Illinois. As such, Taxpayer believes that its Illinois sales should not be included in the numerator of the Indiana sales factor under IC § 6-3-2-2(n).

Taxpayer states that the presence of its returnable containers in the state of Illinois constitutes "doing business in another state" under 45 IAC 3.1-1-38(5). Further, Taxpayer explains that it "rendered services to Illinois customers by presenting a [product] findings presentation and performing vendor audits. Vendor audits involved [Taxpayer] employees visit[ing] Illinois to review vendor products that were used by [Taxpayer] in its production process. The employees performed quality assurance reviews of vendor products to ensure customers received an acceptable product."

In the administrative hearing, Taxpayer provided evidence that during 2014, it had at least one employee work from a home office in Illinois. According to the audit report, employees working in states outside of Indiana are

"account representatives" whose job is to "maintain contact with ongoing and potential customers." These employees work with customers with delinquent accounts, are present while customers dispose of obsolete inventory, are involved with contract negotiations, and communicate to customers whether or not an order is approved.

Illinois imposes a tax upon "every individual, corporation, trust and estate for each taxable year ending after July 31, 1969 on the privilege of earning or receiving income in or as a resident of this State." 35 Ill. Comp. Stat. § 5/201(a). Illinois regulations expound upon what sort of activities establish sufficient nexus with Illinois to subject a taxpayer to Illinois income tax. The regulations refer to "federal statutes regulating interstate commerce . . . United States Constitutional jurisprudence, and [] Illinois tax statutes," for standards in determining sufficient tax nexus. Ill. Admin. Code tit. 86, § 100.9720(b). The regulations also reference P.L. 86-272 as a federal statute that limits Illinois' ability to impose income tax. Ill. Admin. Code tit. 86, § 100.9720(c).

Under P.L. 86-272 and Illinois law, a nonresident taxpayer is only subject to Illinois income tax if the income it derives in Illinois is from activities that exceed solicitation of sales. Unprotected activities, or those activities which subject a taxpayer to Illinois income tax include, but are not limited to:

1. Making repairs or providing maintenance or service to the property sold or to be sold.
2. Providing any kind of technical assistance or services, including, but not limited to, engineering assistance or design service, when one of the purposes of the assistance or service is other than the facilitation of the solicitation of orders.
3. Investigating, handling, or otherwise assisting in resolving customer complaints, other than mediating direct customer complaints when the sole purpose of such mediation is to ingratiate the sales personnel with the customer.
4. Owning, leasing, or maintaining . . . [A s]tock of goods other than samples for sales personnel or that are used entirely ancillary to solicitation.

Ill. Admin. Code tit. 86, § 100.9720(c)(4)(A), (F), (G), and (O)(vi).

If Taxpayer conducted any of the above activities in Illinois, it is subject to Illinois tax. In its protest letter Taxpayer states that it maintained a stock of goods in Illinois by having its products in returnable containers at customer sites in Illinois. Taxpayer also claims that its presentation of product study findings to customers constitutes "providing technical assistance." Taxpayer asserts that it "prepared Audit Summary Reports for vendors with products that did not meet [Taxpayer] quality standards. These products are repaired so that they can be used in [Taxpayer] production processes in the future." Taxpayer believes that these vendor audits "preemptively resolve potential customer complaints."

To support its claims, Taxpayer provided internal travel logs and business trip applications for 2014, an "Account Representative" job description for Illinois, and an "Audit Summary Report" for 2015. While these purport to show that Taxpayer traveled to Illinois to conduct vendor audits, the documentation lacks external proof such as travel receipts, rental agreements, flight confirmations, etc. to substantiate the claims. Further, the dates listed on the travel logs and business trip applications do not match with the dates of the Audit Summary Report. The Audit Summary Report describes some testing activities, but also states that "[n]o onsite testing [was] done. All samples are collected at the end of the day and transferred to [vendor] for analysis." Therefore, while it may be that samples were taken for testing purposes, it appears that the vendor performs the testing.

In 2014 Taxpayer claims to have had returnable containers in Illinois, presented product study findings in Illinois, performed vendor audits in Illinois, and performed quality assurance reviews in Illinois. Additionally Taxpayer had an employee in Illinois working from a home office, whose job was to maintain customer relationships, solicit sales, work with delinquent accounts, be present while customers dispose of obsolete inventory, be involved in contract negotiations, and communicate whether customer orders were approved. As mentioned above, the Department does not find the presence of returnable containers akin to owning property in a given jurisdiction. Taxpayer has not provided evidence that the returnable containers were leased/rented by the customer and the temporary nature of the containers' presence does not lend itself to creating nexus.

Further, the actions of Taxpayer's Illinois employee, like the actions in *Kimberly*, were "inextricably related to solicitation" or as "acts of courtesy," and thus not enough to subject Taxpayer to Illinois income tax. However, if Taxpayer performed activities such as quality assurance reviews and vendor audits, in Illinois in 2014, Taxpayer may have availed itself to Illinois tax as those types of activities are like those in *Wrigley*, in that they took place *because* of a sale and were not "inextricably related to solicitation." Ultimately, Taxpayer has failed to prove that those activities were performed by Taxpayer employees or that those activities were performed in 2014. Thus the

Department cannot sustain Taxpayer in regards to its Illinois sales. Taxpayer is denied; its 2014 Illinois sales were properly thrown back to Indiana.

Louisiana

The Department determined that Taxpayer's sales made to Louisiana were incorrectly excluded from the Indiana sales factor numerator for tax year 2013. Taxpayer argues that it was conducting business in Louisiana under Louisiana law and therefore was taxable in Louisiana. As such, Taxpayer believes that its 2013 Louisiana sales should not be included in the numerator of the Indiana sales factor under IC § 6-3-2-2(n).

Taxpayer states that the presence of its returnable containers in the state of Louisiana constitutes "doing business in another state" under 45 IAC 3.1-1-38(5). However, the Department does not find the presence of returnable containers akin to owning property in a given jurisdiction. Taxpayer has not provided evidence that the returnable containers were leased/rented by their customers and the temporary nature of the containers' presence does not lend itself to creating nexus in Louisiana.

In addition to the returnable containers, Taxpayer noted that it had an employee living in Louisiana and working out of a home office during 2014. According to the audit report, employees working in states outside of Indiana are "account representatives" whose job is to "maintain contact with ongoing and potential customers." These employees work with customers with delinquent accounts, are present while customers dispose of obsolete inventory, are involved with contract negotiations, and communicate to customers whether or not an order is approved. The audit report also notes that only Taxpayer's 2013 Louisiana sales were thrown back to Indiana. The evidence shows that Taxpayer did not have an employee living and working in Louisiana in 2013, thus the presence of an employee in 2014 does not affect this analysis.

Taxpayer makes no argument regarding services rendered in Louisiana in 2013. The bulk of Taxpayer's argument is related to their Louisiana employee (who isn't in the payroll records provided until tax year 2015). Therefore, the only contact that Taxpayer had with Louisiana in 2013, other than sales, was the existence of returnable containers.

Louisiana imposes a tax that "shall be levied, collected, and paid for each taxable year . . . upon the Louisiana taxable income of corporations and other entities taxed as corporations for federal income tax purposes. . . ." La. Rev. Stat. Ann. § 47:287.11(A). However, "[i]f the taxpayer is not taxable in a state to which a sale is assigned or if the state of assignment cannot be determined or reasonably approximated . . . the sale shall be excluded from the numerator and the denominator of the sales factor." La. Rev. Stat. Ann. § 47:287.95(M). Louisiana's regulations flesh out what types of activities are attributable to Louisiana. According to the regulations, "[s]ales made in the regular course of business attributable to Louisiana . . . are those sales where goods, merchandise or property are received in Louisiana by the purchaser." La. Admin. Code tit. 61, Pt. 1, §1134(D)(3)(a)(2005). Further:

> Where the goods are delivered by the seller in his own equipment, it is presumed that such transportation relates to the sale. Where the goods are delivered by a common or contract carrier, whether shipped F.O.B. shipping point, and whether the carrier be a pipeline, trucking line, railroad, airline or some other type of carrier, the place where the goods are ultimately received by the purchaser after the transportation by the carrier has ended is deemed to be the place where the goods are received by the purchaser.
>
> *Id*. at (D)(3)(b).

Therefore, under Louisiana law, depending on where Taxpayer's products were shipped, Taxpayer may be subject to Louisiana corporate income tax. However, Taxpayer did not provide documentation indicating how its products were shipped and where its customers took delivery of the product. As such, the Department cannot determine if Taxpayer is subject to the Louisiana corporate income tax.

In addition to the corporate income tax, Louisiana also has a corporate franchise tax. A franchise tax is defined as "[a] tax imposed on the privilege of carrying on a business ([especially] as a corporation), [usually] measured by the business' income." Black's Law Dictionary 1497 (10th ed. 2014). Louisiana has a corporation franchise tax under which, "[e]very domestic corporation and every foreign corporation, exercising its charter, or qualified to do business or actually doing business in this state, or owning or using any part or all of its capital, plant, or any other property in this state, . . . shall pay an annual tax. . . ." La. Rev. Stat. Ann. § 47.601(A). The tax is measured by "taxable capital," and is due when activities such as the following occur:

> 1. The qualification to carry on or do business in [Louisiana] or the actual doing of business within [Louisiana] in a corporate form. The term "doing business" . . . shall mean and include each and every act, power, right, privilege, or immunity exercised or enjoyed in [Louisiana], as an incident to or by virtue of the powers and privileges acquired by the nature of such organizations, as well as, the buying, selling, or procuring of services or property.
> 2. The exercising of a corporation's charter or the continuance of its charter within [Louisiana].
> 3. The owning or using any part or all of its capital, plant, or other property in this state in a corporate capacity.
>
> La. Rev. Stat. Ann. § 47:601(A)(1), (2), and (3).

Indiana Code § 6-3-2-2(n)(1) states that a taxpayer is taxable in another state if, in that state, Taxpayer is subject to a franchise tax measured by net income or a franchise tax for the privilege of doing business. In *Welch Packaging Group, Inc. v. Indiana Dept. of State Revenue*, 876 N.E.2d 819 (Ind. Tax Ct. 2007), Welch Packaging, an Indiana corporation, had a subsidiary, Barger Packaging Corporation ("BPC"), which "employed salespeople who solicited business in, and delivered products to, the state of Michigan." As a result, BPC was subject to Michigan's Single Business Tax ("MSBT"), and in fact, Welch excluded the Michigan sales from the numerator of their sales factor. The Department audited Welch and determined that the Michigan sales should have been included in the numerator because "[while t]he MSBT may be a tax on the privilege of doing business in Michigan, [ ] it is not a *franchise* tax on the privilege of doing business in Michigan." On appeal, the Indiana Tax Court found that IC § 6-3-2-2(n)(1) "clearly provides that the franchise tax may be measured by either net income or by some other standard." Thus, the MSBT was a franchise tax and, under IC § 6-3-2-2(n)(1), "Welch was not required to include its Michigan sales in the numerator of its sales factor. . . ."

Taxpayer argues that it is "doing business in [Louisiana] because it is qualified to do business in Louisiana, based on its registration on May 14, 2014 with the Louisiana Secretary of State and has an employee that solicits sales in Louisiana." The Department finds this reasoning untenable. The only income at issue here is that which was earned in 2013; Taxpayer's activities in Louisiana in 2014 going forward have no bearing on 2013. Taxpayer has provided no evidence that it paid Louisiana Franchise Tax in 2013. In fact, the only Louisiana tax return Taxpayer provided was for tax year 2015. However, under IC § 6-3-2-2(n)(2) a taxpayer's income is taxable in another state if in that state taxpayer is subject to a franchise tax for the privilege of doing business regardless of whether the other state actually imposes that tax on the taxpayer.

Taxpayer had income in Louisiana in 2013 from the sales of its products. Thus, Taxpayer was subject to the Louisiana corporate franchise tax under La. Rev. Stat. Ann. § 47:601(A)(1). It is not clear whether Louisiana subjected Taxpayer to its franchise tax in 2013, but for Indiana throw-back purposes, that is a moot point. Because Taxpayer was subject to Louisiana's corporate franchise tax in 2013, their 2013 sales were properly excluded from the Indiana sales factor numerator. Taxpayer is sustained in regards to their 2013 Louisiana sales.

New York

The Department determined that Taxpayer's New York sales were incorrectly excluded from the Indiana sales factor numerator for tax years 2013, 2014, and 2015. Taxpayer contends that it was doing business in New York under New York law and therefore was taxable in New York. As such, Taxpayer believes that its New York sales should not be included in the numerator of the Indiana sales factor under IC § 6-3-2-2(n).

Taxpayer states that the presence of its returnable containers in the state of New York constitutes "doing business in another state" under 45 IAC 3.1-1-38(5). However, as mentioned above, the Department does not find the presence of its returnable containers in any state sufficient to create nexus in that state. Taxpayer also explains that "[Taxpayer] rendered services to New York customers by discussing forklift production and customer operations." Taxpayer did not have any employees living and working in New York for the years at issue. Taxpayer supports its position by providing a 2015 job description for a "National Account Representative" to be based in California. Taxpayer also provided internal travel logs showing travel to "New Jersey/New York" in October of 2015. This was accompanied by a business trip application for travel to "New Jersey/NY" for the same dates. Finally, Taxpayer provided a copy of all of their state and local tax returns filed for the years at issue, and it appears that Taxpayer did not file a New York return in 2013 or 2014, but did file one in 2015.

Under New York law:

> For the privilege of exercising its corporate franchise, or of doing business, or of employing capital, or of owning or leasing property in this state in a corporate or organized capacity, or of maintaining an office in this

> state, or of deriving receipts from activity in this state, for all or any part of each of its fiscal or calendar years, every domestic or foreign corporation, except corporations specified in subdivision four of this section, shall annually pay a franchise tax, upon the basis of its business income base, or upon such other basis as may be applicable as hereinafter provided. . . .
>
> N.Y. Tax Law § 209(1)(a).

New York's regulations expand and explain the statute, stating that the New York franchise tax:

> [I]s imposed on every foreign corporation . . . whose activities include one or more of the following:
>
> i. doing business in New York State in a corporate or organized capacity or in a corporate form; or
> ii. employing capital in New York State in a corporate or organized capacity or in a corporate form; or
> iii. owning or leasing property in New York State in a corporate or organized capacity or in a corporate form; or
> iv. maintaining an office in New York State.
>
> 20 NYCRR § 1-3.2(a)(1).

Further, "[a] foreign corporation engaged in New York State in any one or more of [these activities] is subject to tax regardless of whether it is authorized to do business in New York State." 20 NYCRR § 1-3.2(a)(4). However, the regulations refer to Public Law 86-272 stating that a Taxpayer is not subject to tax if its activities amount to "solicitation of orders by the corporation's employees, representatives or independent contractors for sales of tangible personal property, which orders are sent outside New York State for approval or rejection, and, which if approved, are filled by shipment or delivery from a point outside New York State." 20 NYCRR § 1-3.2(a)(3). The regulations concede that "[w]hether a corporation is doing business in New York State is determined by the facts in each case." 20 NYCRR § 1-3.2(b)(2).

Taxpayer may be subject to New York's franchise tax if its activities exceed the protection of Public Law 86-272. Taxpayer did not have employees in New York for the years at issue. Other than solicitation of sales, its only activities in New York were the discussion of both customer forklift productions and customer operations. It is possible that, like those activities in *Wrigley*, these activities are not ancillary to sales and therefore were protected under Public Law 86-272. However, Taxpayer has not provided documentation to show that these discussions did in fact take place by Taxpayer's employees who traveled to New York, nor has Taxpayer provided sufficient explanation as to what these activities entailed. Therefore, the Department determines that Taxpayer's New York sales were properly thrown back to Indiana. Taxpayer is denied in regards to its New York sales.

North Carolina

The Department determined that Taxpayer's sales made to North Carolina were incorrectly excluded from the Indiana sales factor numerator for tax years 2013, 2014, and 2015. Taxpayer argues that it was conducting business in North Carolina under North Carolina law and therefore was taxable in North Carolina. As such, Taxpayer believes that its North Carolina sales should not be included in the numerator of the Indiana sales factor under IC § 6-3-2-2(n).

Taxpayer states that the presence of its returnable containers in the state of North Carolina constitutes "doing business in another state" under 45 IAC 3.1-1-38(5). Further, Taxpayer explains that it "rendered services to North Carolina customers by inspecting customer systems, preparing for [Taxpayer] product tests, and conducting customer training." Further, "[Taxpayer] employees met with customers to discuss product tests for quench oils, hydraulic oils, and coolants."

In the administrative hearing, Taxpayer provided evidence that during the years at issue it had an employee working from a home office in North Carolina. According to the audit report, employees working in states outside of Indiana are "account representatives" whose job is to "maintain contact with ongoing and potential customers." These employees work with customers with delinquent accounts, are present while customers dispose of obsolete inventory, are involved with contract negotiations, and communicate to customers whether or not an order is approved. As proof of its activities in North Carolina, Taxpayer provided meeting minutes from various meetings pertaining to customers in North Carolina in 2013 and 2014. Taxpayer provided internal travel logs and business trip applications involving company cars in 2014 and 2015. Also included in the documentation was an Account Representative job description listing Detroit, Michigan as the office location. Finally, Taxpayer provided copies of the North Carolina income tax returns it filed for the years at issue, each one showing that tax was

owed.

North Carolina imposes a tax "on the State net income of every C corporation doing business in [North Carolina]. . . ." N.C. Gen. Stat. § 105-130.3. Even if a foreign corporation did not obtain a certificate of authority to do business in North Carolina, it may still be liable for North Carolina income tax. 17 N.C. Admin. Code 5C.0101(a). For North Carolina income tax purposes, "the term 'doing business' means the operation of any business enterprise or activity in North Carolina for economic gain. . . ." 17 N.C. Admin. Code 5C.0102(a). This includes:

> (1) the maintenance of an office or other place of business in North Carolina;
> (2) the maintenance in North Carolina of an inventory of merchandise or material for sale, distribution or manufacture, regardless of whether kept on the premises of the taxpayer or in a public or rented warehouse;
> (3) the selling or distributing of merchandise to customers in North Carolina directly from a company-owned or operated vehicle when title to the merchandise is transferred from the seller or distributor to the customer at the time of the sale or distribution;
> (4) the rendering of a service to clients or customers in North Carolina by agents or employees of a foreign corporation;
> (5) the owning, renting, or operating of business or income-producing property in North Carolina. . . .
>
> 17 N.C. Admin. Code 5C.0102(a).

However, "[a] foreign corporation not domesticated in North Carolina whose only activity in [North Carolina] is the solicitation of sales of tangible personal property by either resident or nonresident salesmen is not required to file income tax returns." 17 N.C. Admin. Code 5C.0103.

Taxpayer provided evidence that they had an employee working in North Carolina, but did not provide evidence that the employee's actions in North Carolina went beyond actions that are ancillary to sales. Taxpayer also provided meeting notes and travel logs indicating that Taxpayer employees rendered services to customers in North Carolina. Under North Carolina law, a Taxpayer is doing business in North Carolina if they are rendering services to customers in North Carolina. Thus, because Taxpayer rendered services to customers in North Carolina for the years at issue, its income is taxable in North Carolina and should not be thrown back to Indiana. Taxpayer is sustained as it pertains to its North Carolina sales.

Ohio

The Department determined that Taxpayer's sales made to Ohio were incorrectly excluded from the Indiana sales factor numerator for tax years 2013, 2014, and 2015. Taxpayer argues that it was conducting business in Ohio under Ohio law and therefore was taxable in Ohio. As such, Taxpayer believes that its Ohio sales should not be included in the numerator of the Indiana sales factor under IC § 6-3-2-2(n).

Taxpayer states that the presence of its returnable containers in the state of Ohio constitutes "doing business in another state" under 45 IAC 3.1-1-38(5). Further, Taxpayer explains that it "rendered services to Ohio customers by resolving [] customer complaints concerning [Taxpayer's products]. As part of resolving these customer complaints, [Taxpayer] employees reviewed a testing of new [products] and presented a report on [product] systems."

In the administrative hearing, Taxpayer provided evidence that during the years at issue it had an employee working in Ohio. According to the audit report, employees working in states outside of Indiana are "account representatives" whose job is to "maintain contact with ongoing and potential customers." These employees work with customers with delinquent accounts, are present while customers dispose of obsolete inventory, are involved with contract negotiations, and communicate to customers whether or not an order is approved. As proof of its activities in Ohio, Taxpayer provided internal travel logs, business trip applications, and a job description for an Ohio, Indiana, and Illinois Account Representative. Finally, Taxpayer provided copies of the state and local returns it filed for the years at issue. For all three years, Taxpayer filed returns in two Ohio cities, but did not file an Ohio state return.

Ohio imposes a "commercial activity tax on each person with taxable gross receipts for the privilege of doing business in [Ohio]. . . . '[D]oing business' means engaging in any activity . . . that is conducted for, or results in, gain, profit, or income. . . ." Ohio Rev. Code Ann. §5751.02(A). This tax, called the Commercial Activity Tax or "CAT," is calculated based on a taxpayer's taxable gross receipts. Ohio Rev. Code Ann. §5751.03(A). Taxpayers subject to the CAT, are those "persons with substantial nexus with [Ohio]." *Id.* The term "person" includes companies and for-profit corporations. Ohio Rev. Code Ann. §5751.01(A). A person has substantial nexus with

Ohio if the person:

(1) Owns or uses a part or all of its capital in [Ohio];
(2) Holds a certificate of compliance with the laws of [Ohio] authorizing the person to do business in [Ohio];
(3) Has bright-line presence in [Ohio];
(4) Otherwise has nexus with [Ohio] to an extent that the person can be required to remit the tax. . . .

Ohio Rev. Code Ann. §5751.01(H).

Taxpayer did not address whether it had a certificate of compliance for Ohio authorizing it do business there during the years at issue. Therefore, to determine whether or not Taxpayer had substantial nexus with Ohio during those years, we look to "bright-line presence." A person has "bright-line presence" in Ohio for a reporting period if the person:

(1) Has at any time during the calendar year property in this state with an aggregate value of at fifty thousand dollars. . . .[O]wned property is valued at original cost and rented property is valued at eight times the net annual rental charge.
(2) Has during the calendar year payroll in this state of at least fifty thousand dollars. Payroll in [Ohio] includes all of the following:
  (a) Any amount subject to withholding by the person . . . ;
  (b) Any other amount the person pays as compensation to an individual under the supervision or control of the person for work done in [Ohio]; and
  (c) Any amount the person pays for services performed in [Ohio] on its behalf by another.
(3) Has during the calendar year taxable gross receipts of at least five hundred thousand dollars.
(4) Has at any time during the calendar year within [Ohio] at least twenty-five percent of the person's total property, total payroll, or total gross receipts.
(5) Is domiciled in [Ohio] as an individual or for corporate, commercial, or other business purposes.

Ohio Rev. Code Ann. §5751.01(I).

Taxpayer did not provide documentation concerning the value of the returnable containers it had in Ohio during the years at issue, nor did Taxpayer explain whether those returnable containers are rented or provided as a courtesy in the sale. Taxpayer's payroll records show that for 2015, Taxpayer did have over fifty thousand dollars in payroll, but it did not for 2013 and 2014. Therefore, for 2015, Taxpayer is subject Ohio's CAT tax because its payroll was sufficient enough to give Taxpayer substantial nexus with Ohio under the "bright-line presence" test. For all three years at issue, Taxpayer had over $30 million in sales in Ohio; well beyond the required gross receipts of five hundred thousand to establish nexus and thus taxability in Ohio. Therefore, the Department determines that Taxpayer's sales are taxable in Ohio and should not be thrown back to Indiana. Taxpayer is sustained in regards to their Ohio sales.

Tennessee

The Department determined that Taxpayer's sales made to Tennessee were incorrectly excluded from the Indiana sales factor numerator for tax years 2013, 2014, and 2015. Taxpayer argues that it was conducting business in Tennessee under Tennessee law and therefore was taxable in Tennessee. As such, Taxpayer believes that its Tennessee sales should not be included in the numerator of the Indiana sales factor under IC § 6-3-2-2(n).

Taxpayer states that the presence of its returnable containers in Tennessee constitutes "doing business in another state" under 45 IAC 3.1-1-38(5). Further, Taxpayer explains that it "rendered services to Tennessee customers by performing product trial tests and conducting trainings." Taxpayer supported its claims by providing internal business trip applications and travel logs for 2015, which show that Taxpayer employees traveled to Tennessee to conduct training and product trials. Additionally, Taxpayer provided copies of the Tennessee Franchise and Excise Tax Returns it filed in 2014 and 2015.

Under Indiana law, these activities alone are not enough to protect Taxpayer's sales from throw back. The temporary presence of Taxpayer's returnable containers in Tennessee, the product trials and the trainings are ancillary to the solicitation of sales; they serve no independent business function apart from their connection to the soliciting of orders. *Wrigley.* Therefore, Taxpayer's Tennessee sales are only protected from throw back if Taxpayer was doing business in Tennessee and was subject to Tennessee's tax regime. IC § 6-3-2-2(n).

Doing business in Tennessee is a taxable privilege. Tenn. Code Ann. § 67-4-2005. All persons doing business in

Tennessee and having a substantial nexus in Tennessee must pay an excise tax based on net earnings. Tenn. Code Ann. § 67-4-2007(a). Doing business in Tennessee "means any activity purposefully engaged in within Tennessee, by a person with the object of gain, benefit, or advantage. . . ." Tenn. Code Ann. § 67-4-2004(14)(A). A "person" includes "every corporation." Tenn. Code Ann. § 67-4-2004(38). The tax is imposed "as a recompense for the protection of [a taxpayer's] local activities and as compensation for the benefits [a taxpayer] receives from doing business in Tennessee. . . ." Tenn. Code Ann. § 67-4-2007(b). This tax is imposed regardless of whether a taxpayer is incorporated in Tennessee, domiciled in Tennessee, qualified, or otherwise registered to do business in Tennessee. *Id*. Further, Tennessee imposes an annual franchise tax on "[a]ll persons doing business in [Tennessee] and having substantial nexus in [Tennessee]. . . ." Tenn. Code Ann. § 67-4-2105. The tax is measured based on a taxpayer's net worth. Tenn. Code Ann. § 67-4-2106.

Tennessee's excise and franchise taxes are imposed upon taxpayers who partake in activities in Tennessee for the purpose of gain, benefit or advantage. Taxpayer's sales and other activities in Tennessee fall into this category, therefore, Taxpayer is subject to tax in Tennessee and its sales for the tax years at issue should not be thrown back to Indiana. Taxpayer is sustained in regards to its Tennessee sales.

Texas

The audit determined that Taxpayer's Texas sales were incorrectly excluded from the Indiana sales factor numerator for tax years 2013, 2014, and 2015. Taxpayer argues that it was doing business in Texas under Texas law and therefore was taxable in Texas. As such, Taxpayer believes that its Texas sales should not be included in the numerator of the Indiana sales factor under IC § 6-3-2-2(n).

Taxpayer states that the presence of its returnable containers in Texas constitutes "doing business in [another] state" under 45 IAC 3.1-1-38(5). Further, Taxpayer explains that it "rendered services to Texas customers by providing testing and machine removal services. Employees visited customers in Texas to test machinery for quality assurance purposes, assist in removing machinery, and present findings on machinery review." Taxpayer supported its claims by providing 2015 internal travel logs, 2015 business trip applications, minutes from a 2015 meeting regarding "tear downs," pictures of machinery, and a job description for an account representative based out of California. Taxpayer also filed Franchise Tax Reports in Texas for all three years at issue. In 2013 and 2014, Taxpayer apportioned zero income to Texas and paid no tax. In 2015, Taxpayer did apportion income to Texas, paying a franchise tax of approximately $40,000. Finally, Taxpayer provided proof that they had payroll from an employee operating out of his home in Texas in 2015. According to the audit report, employees working in states outside of Indiana are "account representatives" whose job is to "maintain contact with ongoing and potential customers." These employees work with customers with delinquent accounts, are present while customers dispose of obsolete inventory, are involved with contract negotiations, and communicate to customers whether or not an order is approved.

Under Indiana law, these activities alone are not enough to protect Taxpayer's sales from throw back. The temporary presence of Taxpayer's returnable containers in Texas, the machinery tests and removals are ancillary to the solicitation of sales; they serve no independent business function apart from their connection to the soliciting of orders. *Wrigley.* Therefore, Taxpayer's Texas sales are only protected from throw back if Taxpayer was doing business in Texas and was subject to Texas' tax regime. IC § 6-3-2-2(n).

Under Texas law, "[a] franchise tax is imposed on each taxable entity that does business in [Texas] or that is chartered or organized in [Texas]." Tex. Tax Code § 171.001(a). A "taxable entity" includes corporations. Tex. Tax Code § 171.0002(a). The tax imposed on a taxable entity is based on "taxable margin." Tex. Tax Code § 171.002(a). Texas' franchise tax is incurred for "doing business" in Texas. An entity is conducting business in Texas if its activities ". . . include one or more active operations that form a part of the process of earning income or profit [ ] and the entity performs active management and operational functions." Tex. Tax Code §171.0004(b). Texas administrative code explains:

Some specific activities which subject a taxable entity to Texas franchise tax include, but are not limited to, the following:

1. contracting: performance of a contract in Texas regardless of whether the taxable entity brings its own employees into the state, hires local labor, or subcontracts with another;
2. delivering: delivering into Texas items it has sold;
3. employees or representatives: having employees or representatives in Texas doing the business of the taxable entity;
4. services, including, but not limited to the following:

a. providing any service in Texas, regardless of whether the employees, independent contractors, agents, or other representatives performing the services reside in Texas;
b. maintaining or repairing property located in Texas whether under warranty or by separate contract;
c. installing, erecting, or modifying property in Texas;
d. investigating, handling or otherwise assisting in resolving customer complaints in Texas.

5. solicitation: having employees, independent contractors, agents, or other representatives in Texas, regardless of whether they reside in Texas, to promote or induce sales of the foreign taxable entity's goods or services;

Tex. Admin. Code § 3.586(c)(3), (4), (5), (16)(A), (B), (C), (F), (19).

Taxpayer's activities fall within the activities which subject an entity to the Texas franchise tax for the years at issue. Taxpayer did file Texas franchise tax returns for all three years at issue, however, for 2013 and 2014 Taxpayer's Texas apportionment factor was zero. For those years, a taxpayer's taxable margin was allocated to Texas using an apportionment formula or fraction, "the numerator of which is the taxable entity's gross receipts from business done in [Texas] . . . the denominator of which is the taxable entity's gross receipts from its entire business. . . ." Tex. Tax Code § 171.106(a). In 2013 and 2014, Taxpayer had a positive margin, but listed zero receipts in Texas. Because Taxpayer failed to pay franchise tax in Texas, its 2013 and 2014 sales should be thrown back to Indiana. Had Taxpayer apportioned sales to Texas, the Indiana throw-back rule would not be applied here. Taxpayer is sustained in regards to 2015 but denied for 2013 and 2014.

Virginia

The Department's audit determined that Taxpayer's Virginia sales were incorrectly excluded from the Indiana sales factor numerator for tax years 2013, 2014, and 2015. Taxpayer claims that it was doing business in Virginia and was taxable under Virginia law. As such, Taxpayer believes that its Virginia sales should not be included in the numerator of the Indiana sales factor under IC § 6-3-2-2(n).

Taxpayer states that the presence of its returnable containers in Virginia constitutes "doing business in [another] state" under 45 IAC 3.1-1-38(5). Further, Taxpayer explains that it "rendered services to Virginia customers by discussing and resolving customer complaints. For example, [a Taxpayer] employee traveled to Virginia to respond to a customer complaint regarding [Taxpayer's product]." Taxpayer supported its claims by providing 2013 meeting minutes from a meeting with a customer discussing potential sales, 2014 and 2015 internal travel logs and business trip applications, and a sales job description. Taxpayer also filed a Virginia Corporate Income Tax Return for all three years, reporting tax each year. Taxpayer did not have payroll in Virginia for any of the tax years at issue.

Under Indiana law, these activities alone are not enough to protect Taxpayer's sales from throw back. The temporary presence of Taxpayer's returnable containers in Virginia, and travel to Virginia to discuss and resolve customer complaints are ancillary to the solicitation of sales; they serve no independent business function apart from their connection to the soliciting of orders. *Wrigley.* Therefore, Taxpayer's Virginia sales are only protected from throw back if Taxpayer's activities subjected them to Virginia tax. IC § 6-3-2-2(n).

Generally, Virginia imposes a tax "on the Virginia taxable income for each taxable year of every corporation organized under the laws of [Virginia] and every foreign corporation having income from Virginia sources." Va. Code Ann. § 58.1-400. Every corporation organized under Virginia law or having income from Virginia sources must file a return. Va. Code Ann. § 58.1-441. The Virginia corporate income tax is imposed and the return is required "regardless of whether or not [a] foreign corporation has registered with [Virginia] and obtained a certificate of authority to transact business in Virginia." 23 Va. Admin. Code § 10-120-70. However, Virginia recognizes that "U.S. Public Law 86-272 (15 USC §§ 381-384) prohibits [the state] from taxing income from Virginia sources if the corporation does not have sufficient connection with Virginia." 23 Va. Admin. Code § 10-120-310(A)(4). However, "Corporations whose income from Virginia sources is not subject to tax because of P.L. 86-272 must file a return if they are registered with the [Virginia] State Corporation Commission for the privilege of doing business in Virginia." *Id*.

While Taxpayer's actions in Virginia do not create sufficient nexus with Virginia to subject it to Virginia income tax, the Department was able to determine that Taxpayer is actively registered with the Virginia State Corporation Commission as of March of 2014. Therefore, Taxpayer's 2014 and 2015 Virginia sales are subject to Virginia tax while Taxpayer's 2013 sales should be thrown back to Indiana. Taxpayer is sustained in relation to its 2014 and 2015 Virginia sales and denied in relation to its 2013 Virginia sales.

Washington

The Department determined that Taxpayer's Washington sales were incorrectly excluded from the Indiana sales factor numerator for tax years 2013, 2014, and 2015. Taxpayer claims that it was doing business in Washington and was taxable under Washington law. As such, Taxpayer believes that its Washington sales should not be included in the numerator of the Indiana sales factor under IC § 6-3-2-2(n).

Taxpayer states that the presence of its returnable containers in Washington constitutes "doing business in [another] state" under 45 IAC 3.1-1-38(5). Further, Taxpayer explains that it "rendered services to Washington customers by providing quality assurance services. For example, [a Taxpayer] employee traveled to Washington to inspect product performance and detect product issues." Taxpayer supported its claims by providing a job description for an account representative to work out of a home office in Washington. They also provided internal travel logs showing 2015 travel to Washington, and business trip applications detailing that travel. In these business trip applications, the stated purposes of the travel were to establish relationships with companies, discuss new sales or discuss existing products. Taxpayer did not file returns in Washington for the tax years at issue, nor did they have any payroll in Washington.

Under Indiana law, Taxpayer's activities are not enough to protect its sales from throw back. The temporary presence of Taxpayer's returnable containers in Washington, and travel to Washington to explore new sales opportunities or discuss existing products are ancillary to the solicitation of sales; they serve no independent business function apart from their connection to the soliciting of orders. *Wrigley.* Therefore, Taxpayer's Washington sales are only protected from throw back if Taxpayer's activities subjected them to Washington tax. IC § 6-3-2-2(n).

Washington imposes a business and occupation excise tax on "every person that has a substantial nexus with [Washington]." Wash. Rev. Code § 82.04.220(1). The tax is imposed "for the act or privilege of engaging in business activities." *Id*. The tax is measured by applying a formula to a Taxpayer's "value of products, gross proceeds of sales, or gross income of the business. . . ." *Id*. A taxpayer is "engaging in business activities" in Washington when it "generates gross income . . . from sources within [Washington], such as customers or intangible property located in [Washington], regardless of whether the person is physically present in [Washington]. Wash. Rev. Code § 82.04.066. A person doing business in Washington is "deemed to have substantial nexus" with Washington if the person is:

(a) An individual and is a resident or domiciliary of [Washington];
(b) A business entity and is organized or commercially domiciled in [Washington]; or
(c) A nonresident individual or a business entity that is organized or commercially domiciled outside this state, and in any tax year the person has:
  (i) More than fifty thousand dollars of property in [Washington];
  (ii) More than fifty thousand of payroll in [Washington];
  (iii) More than two hundred fifty thousand dollars of receipts from [Washington];
  (iv) At least twenty-five percent of the person's total property, total payroll, or total receipts in [Washington].

Wash. Rev. Code § 82.04.067(1).

Taxpayer is without question engaging in business activities in Washington. The question is whether Taxpayer had substantial nexus with Washington during the years at issue. Taxpayer was not organized or domiciled in Washington. Taxpayer did not have more than fifty thousand dollars of property in Washington, nor did it have more than fifty thousand dollars of payroll in Washington. However, for each year at issue, Taxpayer had over two hundred fifty thousand dollars in sales in Washington. Therefore, Taxpayer had substantial nexus from engaging in business activities in Washington and was subject to Washington tax. Taxpayer is sustained in regards to their Washington sales.

FINDINGS

Taxpayer's sales made in 2013, 2014, and 2015 to Florida, Georgia, Louisiana, North Carolina, Ohio, Tennessee, and Washington, as well as those sales made in 2015 in Texas, and 2014 and 2015 in Virginia should be excluded from the numerator of Taxpayer's apportionment formula. However, Taxpayer's 2013, 2014, and 2015 sales to Canada, Illinois, and New York, as well as those sales made to Texas in 2013 and 2014, and sales made to Virginia in 2013 are properly included in the numerator of Taxpayer's apportionment formula.

II. Tax Administration–Negligence Penalty.

DISCUSSION

Taxpayer protests the imposition of a ten percent negligence penalty pursuant to IC § 6-8.1-10-2.1. Penalty waiver is permitted if Taxpayer shows that the failure to pay the full amount of the tax was due to reasonable cause and not due to negligence. 45 IAC 15-11-2(b) clarifies the standard for the imposition of the negligence penalty as follows:

> "Negligence" on behalf of a taxpayer is defined as the failure to use such reasonable care, caution, or diligence as would be expected of an ordinary reasonable taxpayer. Negligence would result from a taxpayer's carelessness, thoughtlessness, disregard or inattention to duties placed upon the taxpayer by the Indiana Code or department regulations. Ignorance of the listed tax laws, rules and/or regulations is treated as negligence. Further, failure to read and follow instructions provided by the department is treated as negligence. Negligence shall be determined on a case by case basis according to the facts and circumstances of each taxpayer.

The standard for waiving the negligence penalty is given at 45 IAC 15-11-2(c) as follows:

> The department shall waive the negligence penalty imposed under IC 6-8.1-10-1 if the taxpayer affirmatively establishes that the failure to file a return, pay the full amount of tax due, timely remit tax held in trust, or pay a deficiency was due to reasonable cause and not due to negligence. In order to establish reasonable cause, the taxpayer must demonstrate that it exercised ordinary business care and prudence in carrying out or failing to carry out a duty giving rise to the penalty imposed under this section. Factors which may be considered in determining reasonable cause include, but are not limited to:
> (1) the nature of the tax involved;
> (2) judicial precedents set by Indiana courts;
> (3) judicial precedents established in jurisdictions outside Indiana;
> (4) published department instructions, information bulletins, letters of findings, rulings, letters of advice, etc.;
> (5) previous audits or letters of findings concerning the issue and taxpayer involved in the penalty assessment.

Because the question of reasonable cause is a fact sensitive one, the facts and circumstances in each case must be examined. After review, a large portion of the sales which were thrown back in the Department's audit were appropriately excluded from the apportionment numerator in Taxpayer's original calculation. The issue of throw-back sales is a complicated one, but Taxpayer had gave good reasons for its position. Taxpayer has affirmatively established that it exercised ordinary business care in this case. Waiver of penalty is warranted under 45 IAC 15-11-2(c).

FINDING

Taxpayer's protest to the imposition of the negligence penalty is sustained.

SUMMARY

In regards to Issue 1, Taxpayer's 2013, 2014, and 2015 sales made to Florida, Georgia, Louisiana, North Carolina, Ohio, Tennessee, and Washington, as well as Taxpayer's 2015 Texas sales, and 2014 and 2015 Virginia sales should be excluded from the numerator of Company's apportionment formula. However, Taxpayer's 2013, 2014, and 2015 sales to Canada, Illinois, and New York, as well as those sales made to Texas in 2013 and 2014, and sales made to Virginia in 2013 are properly included in the numerator of Company's apportionment formula. The Department's audit division will recalculate Taxpayer's assessments based on these findings. Taxpayer's Issue II protest regarding the imposition of negligence penalty is sustained.

June 11, 2019

Posted: 08/28/2019 by Legislative Services Agency
An html version of this document.